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United States Senate

COMMITTEE ON SMALL BUSINESS & ENTREPRENEURSHIP
WASHINGTON, DC 20510-6350

July 1, 2002

BY FACSIMILE
ORIGINAL BY U.S. MAIL

The Honorable Charles O. Rossotti
Commissioner
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, DC 20224

Mr. Joseph Kehoe
Commissioner
Small Business/Self-Employed Division
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, DC 20224

Dear Commissioners Rossotti and Kehoe:

The Treasury Inspector General for Tax Administration (TIGTA) recently completed a review of the Internal Revenue Service's (IRS) efforts to identify trends in erroneous notices and refunds sent to business taxpayers. I have been following TIGTA's work in this area because I believe it provides an avenue to identify problems that can be corrected within the agency before small business taxpayers are unnecessarily burdened.

As noted in TIGTA's audit report, "Analysis of Notice Error Trends May Identify Systemic and Procedural Causes for Erroneous Notices and Refunds," (Reference Number 2002-30-095), during calendar year 2000, the IRS sent more than 14 million notices and \$37 billion in refunds to business taxpayers, including small businesses and the self-employed. TIGTA found that during calendar years 2000 and 2001, 32% of the notices reviewed had to be corrected or voided. In addition, the IRS stopped more than 11,000 erroneous refunds totaling over \$132 million in calendar year 2000 and more than 12,000 erroneous refunds totaling over \$316 million in the first 10 months of 2001.

While the agency has systems for reviewing notices, they do not examine 100% of the notices and refunds that the agency issues. In addition, the agency's analysis of the cause of such erroneous notices and refunds has focused primarily on the specific processing center issuing them. TIGTA noted that currently "there is no national trend analysis performed of the error rates reported by the Notice Review functions."

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The agency's review processes can serve as an important source of information for identifying trends in and correcting the root cause of erroneous notices and refunds. In many ways, this issue is similar to small business tax abatements about which I wrote you on March 1, 2002. In both cases, the information can be used to correct systemic and procedural problems before the taxpayer is forced into the picture.

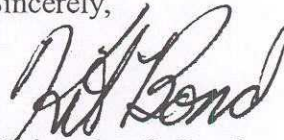
Moreover, given the concerns about the IRS' staffing and funding, information that can reduce the amount of personnel time and effort spent on unnecessary notices and refunds (including the subsequent follow up required in cases in which the erroneous notice or refund in fact reaches the taxpayer) should ease the strain on the agency's resources. If error trends are identified and addressed, additional personnel will be available for more important functions like customer service and compliance.

The TIGTA report notes that the agency has agreed to implement the recommendations set out in the report, and I applaud your willingness to take these steps. I urge you, however, to implement the recommendations as quickly as possible. Waiting until January 1, 2003, as stated in the Management's Response to the Draft Report, is likely to lead to missed opportunities. It should not be a difficult matter to begin reviewing at the national level the notice-error information from the various processing campuses. In addition, testing the feasibility of reviewing voided notices over the next six months seems far more preferable than undertaking such a task during the filing season that begins in early 2003.

Again, thank you for addressing this important issue. Reducing erroneous notices and refunds is a significant service to the taxpayers and only stands to benefit the agency.

If you have any questions or would like to discuss this matter in greater detail, please do not hesitate to contact me or have your staff contact Mark Warren, my Tax Counsel on the Committee on Small Business and Entrepreneurship, at 202/224-

Sincerely,

A handwritten signature in dark ink, appearing to read "Chris Bond", written over a horizontal line.

Christopher S. Bond
Ranking Member